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From:
Sent: Friday, 11 July, 2008 08:21
To:
Cc:
Subject: RE: Need help, oh great one

I marked your incoming.

From:
Sent: Thursday, 10 July, 2008 14:41

To:
Subject: RE: Need help, oh great one

What bothers me the most about this case is the examiner states in the RAR:

[REDACTED] (not exactly the
 term used in RP 2002-28 but close enough that I am guessing that
 is what he is referring to) [REDACTED]

[REDACTED] (when I hear this, I always think § 448) .

[REDACTED] (I could read
 this as saying that the income and expenses must be computed
 using the same MOA) [REDACTED]

[REDACTED] (true statement) "

[REDACTED] (I'll disagree with this point.
 Cash is a MOA allowed by the Code), [REDACTED]

[REDACTED] (I agree. We won't support an attack on the
 cash MOA because he thinks it does not CRI if the taxpayer really
 does fit into the RP). Is this your take? (Reading your quoted paragraph,
 I could nit pick that he didn't close the loop by saying something

like "Therefore, because the taxpayer's cash MOA doesn't [REDACTED] the [REDACTED], this MOA doesn't CRI and thus, pursuant to § 446, the taxpayer may not continue this MOA but must change in 200? to (the/an)? MOA." However, I think he was driving at this. Basically, he is trying to trump the RP with § 446. That makes no sense. If the RP lets someone use the cash MOA, that method will CRI. If that wasn't true, then very few taxpayers could safely use the cash MOA provided by the RP. What can still be attacked though is how the cash MOA is being applied.

I have no information on the breakdown of the GR. That RAR merely states:

[REDACTED]
[REDACTED] (I assume this is the § 1.162-3 idea. If the [REDACTED] qualifies as inventoriable items, the taxpayer is merely agreeing to follow the RP. The RP forces those items to be treated like non incidental M & S) [REDACTED]

[REDACTED] (The RP foresees that there could be more than 1 code #. To see which # to use if there is more than 1, the taxpayer looks at its gross receipts. I know nothing about your taxpayer but I imagine it is someone who buys the furnace, ducts, etc from someone else and then either puts the stuff together at their shop or most likely in someone's basement. To see whether your guy fits into the RP, examples 2, 3 & 4 may help).

My further take is that the taxpayer can remain on the cash method, but now I see why they made the offer to establish a M&S inventory. They can only deduct M&S *when consumed*. I think this is the only thing the TP has done wrong. [REDACTED], **do you agree?** (Yes, if the M & S are inventoriable items as meant by the RP, then there is no doubt. Examples 7 & 8 of the RP may help. Even if they aren't, § 1.162-3 is still out there so if the stuff is not incidental as that term has been understood for almost 90 years, § 1.162-3 forces the costs of the M & S to be capitalized).

One last question which I really never dwelled on before. There is a court case where the government prevailed on a taxpayer who was an HVAC company to be on **an** accrual method. There is also Thompson Electric where an electrical contractor was held to have inventory and therefore required to be on **an** accrual method. But even though these cases are still good law, they are pre-empted by RP 2002-28, the safe harbor. **(Exactly. The RP is an administrative call to not**

pursue this issue for taxpayers that fit into the RP. The cases are still good law.) In essence, it is irrelevant what the ratio of purchases is to gross receipts or whether the income is clearly reflected if the taxpayer fits under RP 2002-28. **(Exactly, if the RP applies. Basically, the GR issue is taken up in section 4.01(1) when the taxpayer has to decide on its NAICS code # and income is going to be clearly reflected if the taxpayer fits into the RP. Of course, the taxpayer has to properly use the RP and included in that idea is that the taxpayer will also properly follow any other applicable Code/law provision. What I am specifically thinking about is what happened with § 1001 when several taxpayers just forgot that § 1001 still applied even if they qualified for & used the RP)** They could have 50% of purchases to gross receipts and still be untouchable if they have a good NAIC. **Correct?** (Interesting. I was wondering if there was exactly a 50-50 split between GR from sales and installation, what would be the code #? As far as the old test of purchases to gross receipts, that test isn't used in the RP). Somehow I never appreciated this before. I guess that's why they call it a safe harbor.

I always appreciate your input.